No. 15,787

In the

United States Court of Appeals

For the Ninth Circuit

UNDERWRITERS SERVICE, INC., a corporation,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Petitioner's Reply Brief

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SUBJECT INDEX

TABLE OF AUTHORITIES CITED

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I.

ARGUMENT

A. General Reply to Arguments of Respondent.

In his brief, Respondent, obviously unwilling to meet directly the specific contentions made by Petitioner in its opening brief, tries to overcome their effect indirectly by arguing in general and extremely vague terms that such contentions are (1) contrary to the purpose and intent of Section 435(d) of the Internal Revenue Code of 1939 and (2) that the language of this section does not warrant the construction for which Petitioner contends. Not wishing to repeat the arguments contained in our opening brief, we shall here attempt to simply answer the arguments utilized by Respondent in support of his position to the extent that

certain aspects thereof may not have been specifically covered in our opening brief.

To support his first point, the Respondent, on pages 8 and 9 of his brief, cites and quotes from the House and Senate reports, the substance of which merely discusses in very general terms the Excess Profits Tax Act of 1950. Nowhere can be found in these reports a specific statement with respect to the particular section or sentence of the Internal Revenue Code here involved, nor indications as to the purpose or intent thereof. By what might be termed "bootstrapping", the Respondent, on pages 18 and 19 of his brief, has attached much significance to a statement of The Tax Court that the second sentence of Section 435(d)(1) was intended to take care of the situation where the taxpayer is in existence for only a part of the beginning month of a taxable year. The fallacy of this argument lies in the fact that this statement was arbitrarily and gratuitously made by The Tax Court, without a shred of support and was simply as good a guess as any as to what situation this sentence was meant to apply.

Moreover, even if we are to assume that this is the situation, or one of them, that this sentence was intended to cover, we would have exactly the same result as Respondent now calls "absurd"—specifically, that the excess profits net income of a taxpayer in that situation would be inflated over that of his actual income by attributing to the beginning part month of a taxable year an amount arrived at by dividing the total income for that particular taxable year by the number of full calendar months in such year. It is quite apparent that it would be not at all unusual for a taxpayer to have an excess profits tax net income double that of his actual net income were he within this assumed situation. This result should not be perfectly all right in one case and "absurd" in another.

The Respondent then argues that the plain language (which he then proceeds to ignore) of Section 435(d)(1) does not warrant the construction contended for by Petitioner, apparently for the simple reason that he feels the result is "unreasonable." He talks again in terms of an imagined purpose, an artificially created standard, and, of course, then has no trouble in concluding that the Petitioner's contention is unwarranted. The advantage of this approach, from the Respondent's standpoint, is that he is thus saved the trouble of answering, or meeting, the arguments of Petitioner with respect to the meaning of the term "taxable year" contained in Section 435(d)(1) and the principles of statutory construction applicable to tax statutes.

Respondent, apparently for lack of an answer, makes no attempt to discuss the application of the term "taxable year" to the situation presented here. This essential cannot be dismissed by simply ignoring it.

Respondent does, inferentially, recognize the problem raised by applying the principles of statutory construction, but it is quite interesting that none of the cases cited, and quoted from, on pages 16-17 of his brief concerned tax statutes. The first, *Johnson v. United States*, 163 Fed. 30 (1908), held that a schedule of assets filed in an involuntary bankruptcy proceeding was a pleading within the meaning of a statute prohibiting the introduction of a pleading as evidence to be used against a defendant.

The second, *Federal Deposit Corp. v. Tremaine,* 133 F.2d 827 (2d Cir. 1943), concerned the meaning to be given the term "public money" in a statute permitting a national bank to pledge its assets as security for a deposit of "public money." Finally, the third, *Cabell v. Markham,* 148 F.2d 737 (2d Cir. 1945), simply held, quite correctly, to say the least, that a complaint filed by a creditor under the Trading with the Enemy Act, as re-enacted for World War II, did

not require as a condition to such suit that the debt be owing on October 6, 1917!

It would appear quite academic to conclude that none of these cases relied on by Respondent are applicable to the construction of a tax statute, and most assuredly cannot be taken as overruling or distinguishing the decisions of The Supreme Court of the United States cited by the Petitioner in its opening brief and *all* of which cases were concerned with the construction of tax statutes.

It is appropriate to also point out that Respondent does not attempt to argue that the principles of statutory construction applicable to statutes in general are equally applicable to tax statutes. As he ignores the language of Section 435(d)(1), Respondent also ignores the language of The Supreme Court of the United States with respect to construing tax statutes. An example of such language, which is at this time well worth repeating, is contained in *Crooks v. Harrelson,* 282 U.S. 55, 61 (1930):

> "Finally, the fact must not be overlooked that we are here concerned with a taxing act, with regard to which the general rule requiring adherence to the letter applies with peculiar strictness."

B. Reply to the Alternative Argument of Respondent with Respect to the Remand of this Case.

The final argument of Respondent is that, if this Court should disagree with the decision of The Tax Court, this case should be remanded for the computation of the excess profits tax credit of Petitioner in a manner which would result in increased deficiencies for the tax years here involved. This argument of Respondent was, of course, rejected by The Tax Court after it sustained the Respondent's deficiency determination.

The basis of Respondent's argument in support of this alternative contention is that Petitioner had no separate existence during the period for which a consolidated return was filed and therefore had only two taxable years during which it had a separate existence, instead of three, during the calendar year 1946. This is a very misleading and erroneous contention, in that, in the first place, the statute is worded in terms of "existence", not "separate existence."

Secondly, "existence", as that term is used in Section 435(d)(1), has no relationship to whether or not consolidated returns are filed. It clearly refers to whether or not a taxpayer is duly incorporated under the laws of some governmental body having authority to create artificial entities. There is no issue as to that fact here.

Finally, Respondent, on page 20 of his brief, makes the completely accurate statement that "a fractional part of a year is a 'Taxable year' only if a return is made for that period." He then draws the completely inaccurate conclusion by saying that, since "no return was filed either by taxpayer or by its parent for the fractional part of the year 1946, taxpayer had—taxwise—no existence for that period." This ignores the fact that, pursuant to the Regulations and the letter, dated April 18, 1947, from Respondent, Petitioner's income for the fractional part of the year during which it was affiliated was returned in its parent's consolidated return and led to Respondent's conclusion in that letter that "each period of less than twelve months for which a separate *or consolidated* return is filed, under the provisions of Section 23.13, shall be considered as a taxable year." (Emphasis added). It is quite anomalous to conclude that a taxpayer has—taxwise—no existence during a period which —taxwise—is one of its three taxable years.

We submit that the sole issue to be decided on this appeal is whether the Petitioner's method of computing its excess profits tax credit is correct or whether The Tax Court was correct in sustaining the Respondent's determination. There is no alternative issue.

II.

CONCLUSION

The Petitioner's position is that the application of the clear language of Section 435(d)(1) to the facts of this case necessarily results in the excess profits tax credit contended for by Petitioner and that the decision of The Tax Court in sustaining the Respondent is incorrect and should be reversed.

Dated: San Francisco, California, May 12, 1958.

Respectfully submitted,

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